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H. DAVID AND DIANE SWAIN CENTER FOR BUSINESS AND ECONOMIC SERVICES

Economic Barometer

SWAIN CENTER PROFESSIONAL AND CONTINUING EDUCATION

Volume VIII Issue I April 2015

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Learn about our benefactors, H. David and Diane Swain at www.csb.uncw.edu/swaincenter

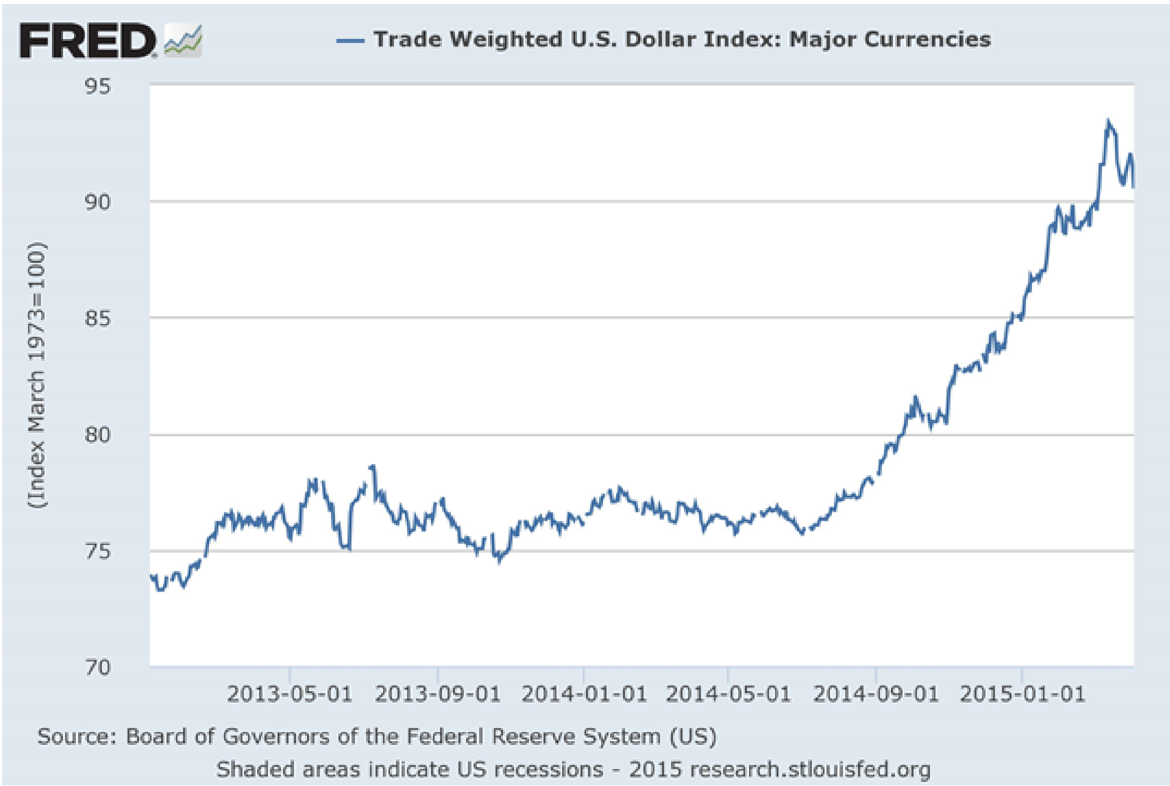
The U.S. Economy

Recent performance. The U.S. economy has been giving off mixed signals thus far in 2015. Employment growth slowed sharply in March to 126 thousand from average monthly gains of 233 thousand in the first two months of the year and 260 thousand per month over all of 2014. In contrast, weekly claims for unemployment insurance through early April have continued to hover near historical lows, as seen in the chart below, suggesting that the labor market remains robust.

Based on spending data used to construct GDP, it appears that growth in real GDP slowed to only a 1 percent annual rate in the first quarter, as shown in the table below.

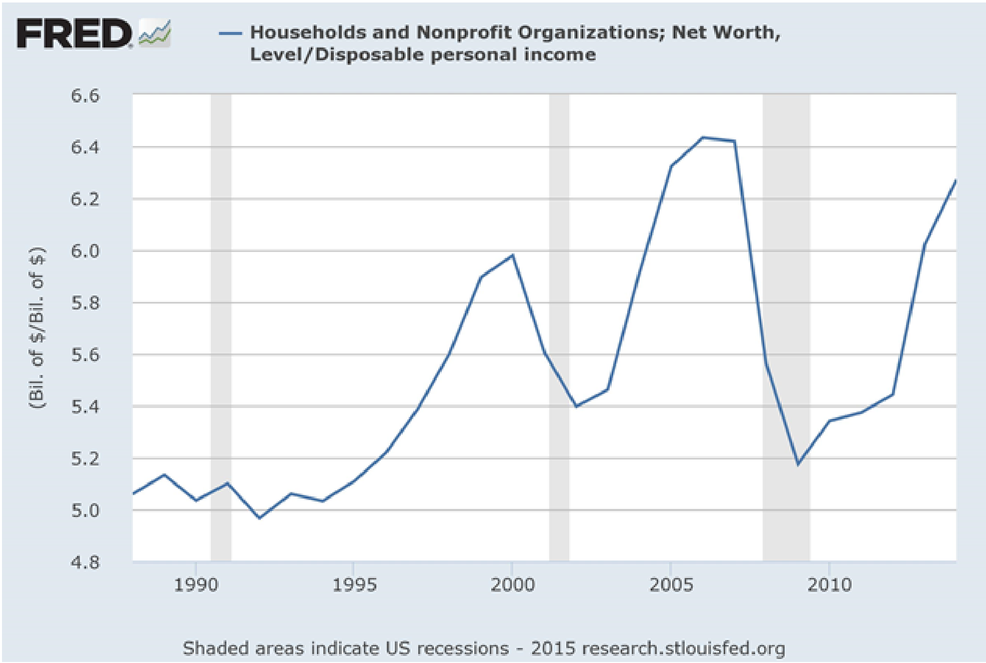
2012	2013	2014	2014	2014	2014	2015
		Q1	Q2	Q3	Q4	Q1^{e}
1.6	3.1	-2.1	4.6	5.0	2.2	1

While unusually harsh winter weather again contributed to the winter slowdown, the stronger dollar, shown below, also has been taking its toll on the external sector, eroding the competitive position of U.S. exports. Absent a quick reversal, the strong dollar is likely to continue to restrain growth over the next few quarters.

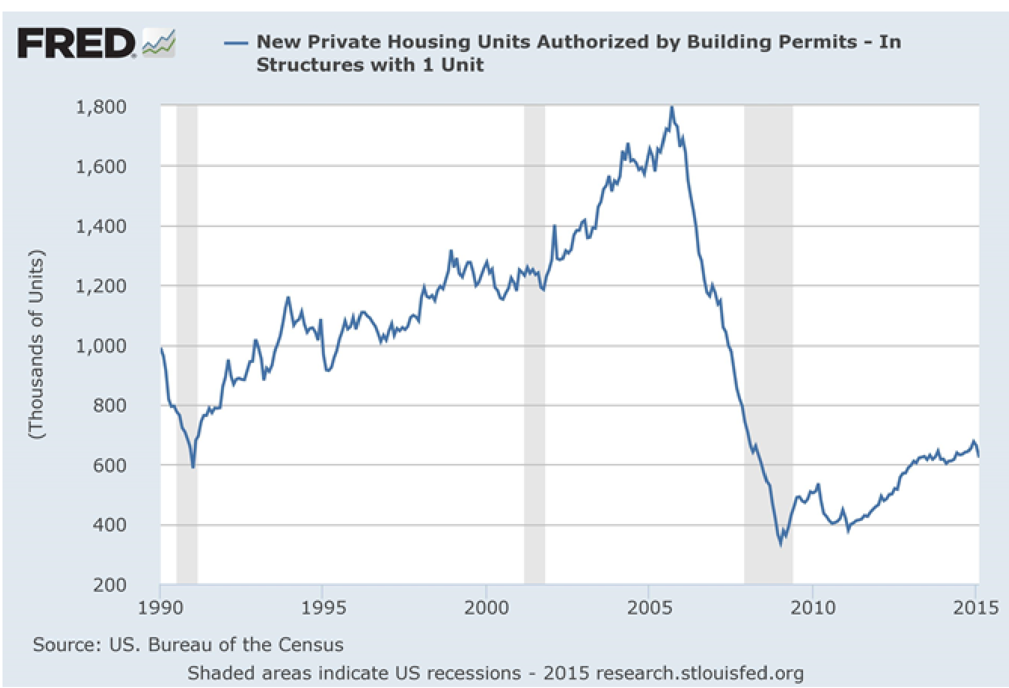


Nonetheless, the conflicting signals given by the labor market data and spending components used to construct GDP may be suggesting that the GDP data are understating actual growth, as often has happened when they have conflicted on various occasions in the past.

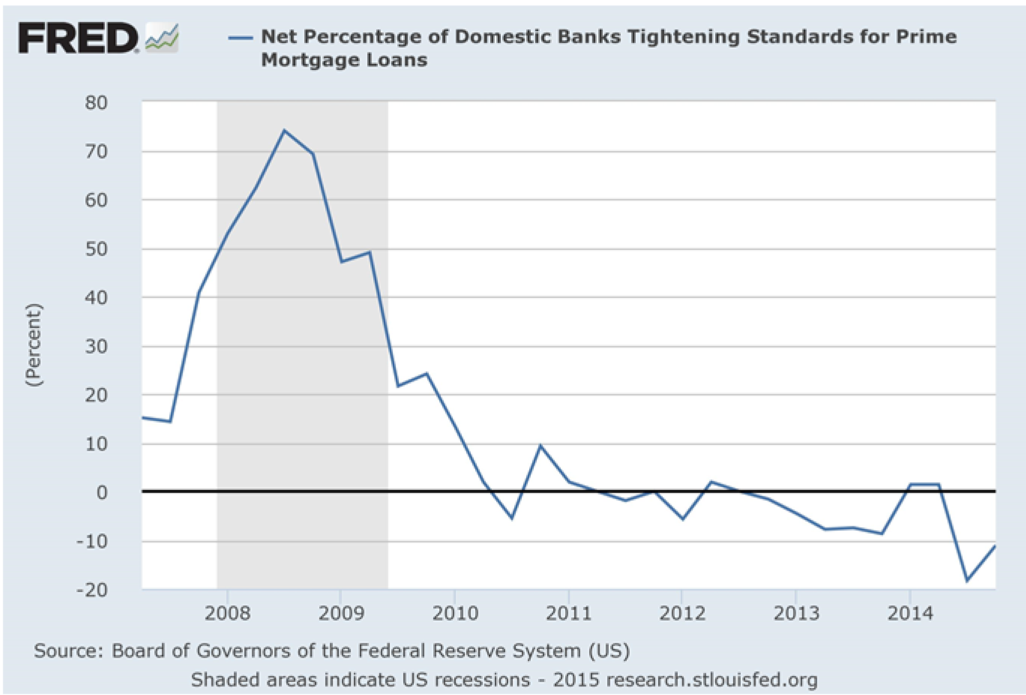
Outlook for growth. Despite near-term headwinds from the external sector, output growth should pick up, paced by household spending. Undergirding household spending will be the extra purchasing power provided by the big drop in gas prices, as well as by earnings from job gainers and wealth generated by rising house prices and the elevated stock market. As shown below, wealth in relation to income has been approaching the highs of recent decades, encouraging households to boost their spending, as they did during the stock market boom of the 1990s and the surge in home prices a decade ago. In these circumstances, consumption outlays should pick up a little from the 3 percent pace of the past year or so.



Moreover, housing activity should also pick up from its moribund state, shown in the chart below illustrating building permits for single-family homes. New home construction has been largely flat over the past year or so and has not improved much from Great Recession lows.

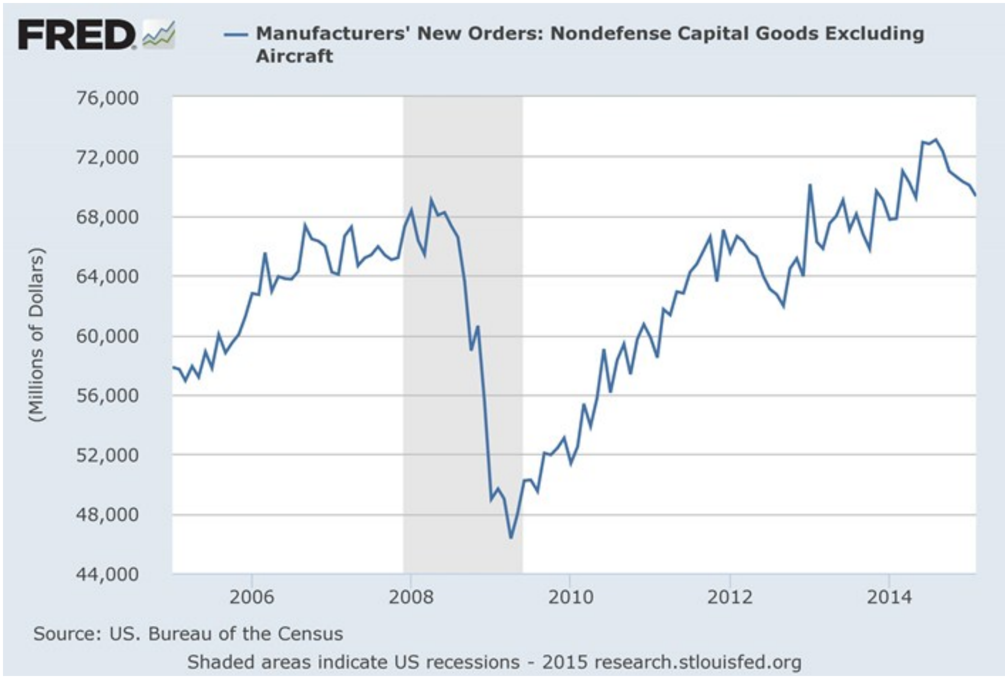


Holding back this sector has been heightened caution by households and restrictive credit conditions, as mortgage originators have been extra cautious in making conforming mortgages that might be put back to them for not meeting standards. However, mortgage originators have been reporting more willingness to make prime mortgages, as seen in the next chart.



Over recent quarters, commercial bank originators of mortgages have become more accommodative—shown by some unwinding of previous very stringent standards. Better credit availability should enable large pent-up housing demands to be translated into more home construction.

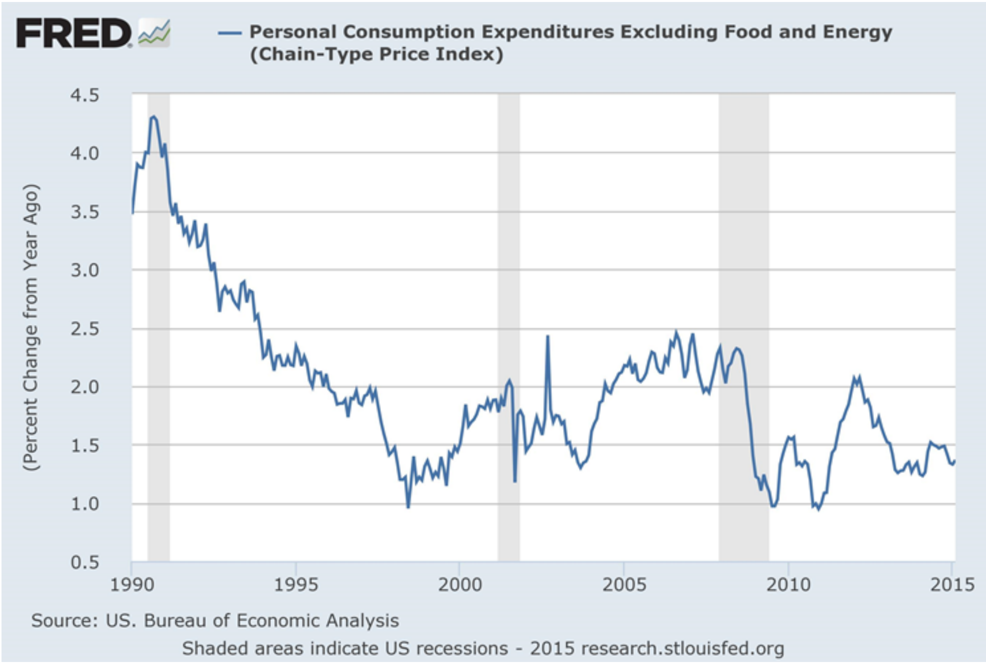
Elsewhere, businesses are expected to remain cautious when it comes to investment, even though there are few restraints holding down business spending. Businesses are holding massive amounts of liquid assets and have ready access to credit on favorable terms, especially in the public bond market. As shown in the chart below, forward looking orders for capital goods (excluding the volatile aircraft component) have turned down over recent months, having been lackluster over the past few years.



Business executives continue to attribute their caution to concerns about the regulatory climate and an unsustainable fiscal situation that portends higher taxes. Public policies to address these concerns are not expected to improve much over the projection period. Similarly, government budgets will not be providing impetus to the economy over the coming years, as the modest restraint coming from the federal budget will be roughly offset by gradually rising outlays by state and local governments.

Putting the pieces together, growth is projected to average nearly a 3 percent pace over the remainder of 2015 and over the following two years. This will be almost 1 percentage point above growth in potential output, which should result in a gradual absorption of slack in resource markets. In these circumstances, employment growth will remain solid and the unemployment rate will drift lower—toward 5 percent.

Inflation and monetary policy. In these circumstances, inflation is expected to remain subdued. The chart below illustrates the Fed's preferred measure of core inflation, the Personal Consumption Expenditures (PCE) index, and shows that core inflation has continued to run below the Fed's target of 2 percent.



To a degree, low inflation readings over recent months reflect the influence of the stronger dollar and also indirect effects of lower energy prices. These are transitory influences, and, even after they disappear, inflation is unlikely to rise much until labor markets have improved further and slack in other resource markets has been removed.

This poses a dilemma for the Fed, which has been signaling to markets that it believes that the time is drawing near for it to begin to normalize monetary policy—lift the federal funds rate from its zero lower bound where it has been since late 2008. The Fed has hinted that initial lift-off could come as early as June, although some officials have suggested September. Of particular concern is whether initial tightening actions when inflation is not clearly on a path to the 2 percent target would cause businesses and households to lower their expectations of inflation. If so, this would put further downward pressure on the actual inflation rate.

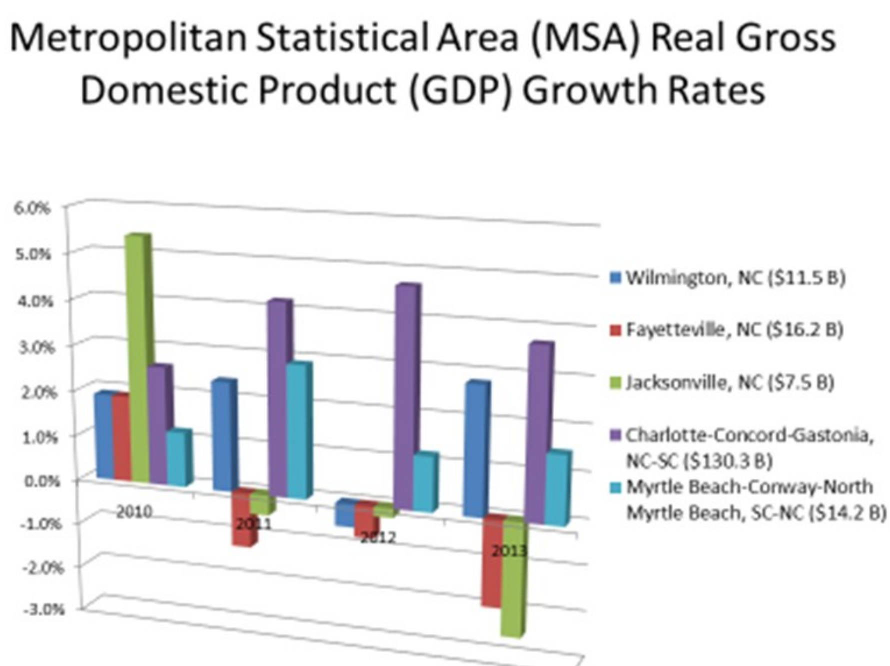
At their March FOMC meeting, Fed officials projected that the federal funds rate would be around 0.6 percent (median forecast) at the end of this year and would increase 1-1/4 percentage points each year over the two years following. This is less than the 2 percentage points per year increases that characterized policy tightening a decade ago—from mid-2004 to mid-2006. In contrast, market participants see a much milder trajectory, with the federal funds rate closing out this year around 0.35 percent and rising about 0.7 percentage points each year over the two subsequent years.

Much discussion in financial markets has focused on how the markets will react to Fed tightening, once it begins. Worries have been fueled by large and volatile market responses to some previous tightening episodes, most notably in the mid-1990s. For its part, the Fed has tried to prevent a repeat of those periods by being more transparent about its thinking. As a consequence, as noted above, the markets have built into asset prices a trajectory of expected Fed moves, which is less aggressive than the Fed's own expectations. Should the timing and trajectory of actual moves be broadly in line with market expectations, we can expect only small-scale market effects once the tightening cycle gets underway.

The Local Economy

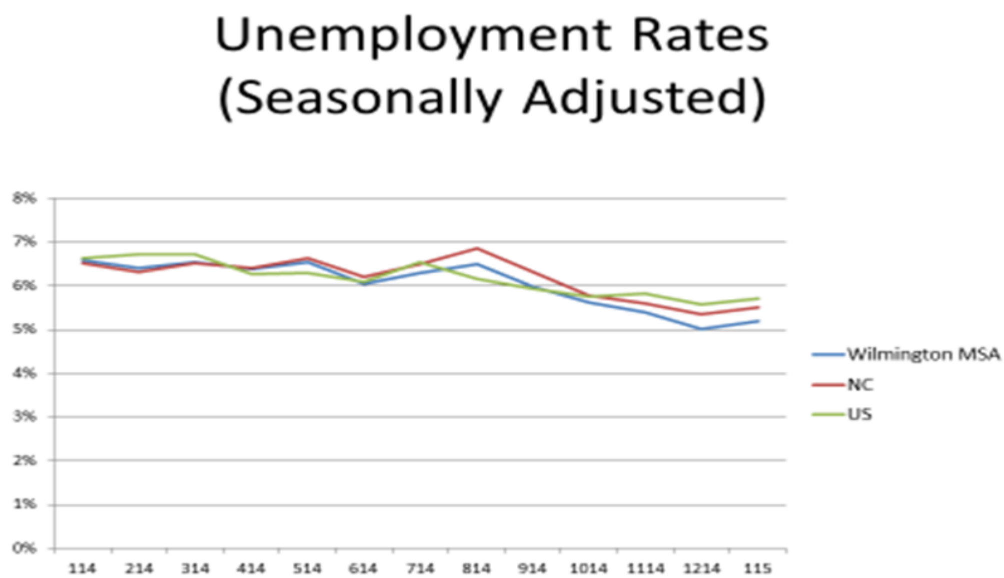
MSA Gross Domestic Product. Revised data on real (inflation-adjusted) gross domestic product (GDP) show that, with the exception of a 1-% decline in 2012, the Wilmington, NC MSA (New Hanover and Pender Counties) economy grew over 2010-13. Real GDP in the MSA is forecast to rise 3.5% over 2014 and 3.8% over both 2015 and 2016. As the 2013 GDP figures in the legend show, the Wilmington, NC MSA was 53% larger than the Jacksonville, NC MSA, 81% as large as the Myrtle Beach-Conway-Georgetown, SC-NC MSA, 71% as large as the Fayetteville, NC MSA, and 9% as large as the Charlotte-Concord-Gastonia NC-SC MSA.

Source: William W. Hall, Jr. for the Swain Center for Business and Economic Services, Cameron School of Business, UNC Wilmington; Bureau of Economic Analysis, U.S. Department of Commerce.



Unemployment. Unemployment rates in the Wilmington MSA have been falling since year-end 2012. Since September 2014, the rate for the MSA has been below that for both the state and the nation. The January 2015 seasonally adjusted MSA rate of 5.2% compares to a January 2014 rate of 6.6% and a January 2013 rate of 9.7%. In sharp contrast, over 2007, the year prior to the start of the 2008-09 national recession, the MSA monthly unemployment rate rarely exceeded 4%.

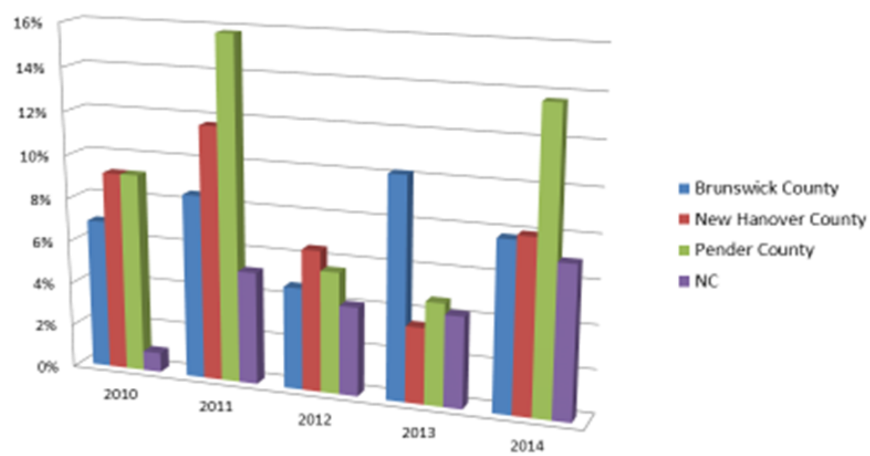
Source: Division of Employment Security, NC Department of Commerce; Bureau of Labor Statistics, US Department of Labor.



Retail Sales. Following strong growth over 2011, retail sales grew at a slower pace throughout most of southeastern North Carolina and the state in both 2012 and 2013. The major exception was retail sales growth of 10.2% in Brunswick County over 2013. Growth was strong in 2014 with Brunswick County sales growing 7.8%, New Hanover County sales growing 8%, Pender County sales growing 13.7%, and North Carolina sales growing 7%. Retail sales in both the local area and state have recovered completely from the hits that they suffered in the 2008-09 national recession.

Source: NC Department of Revenue.

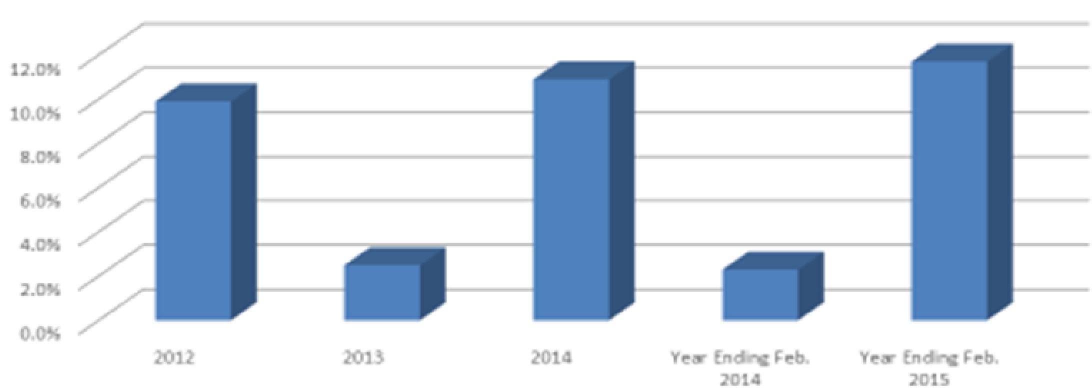
Retail Sales Growth Rates



New Hanover County Room Tax Collections. The tourism sector of the local economy has rebounded to its pre-recession (late-2007) status. Collections from the two 3-% room occupancy taxes levied in New Hanover County rose dramatically in 2011, 2012, and 2014. Although positive, the growth rate over 2013 was only one-fourth the 2012 growth rate. For the year ending February 2015 (March 2014-February 2015), tax revenues were up 11.7%.

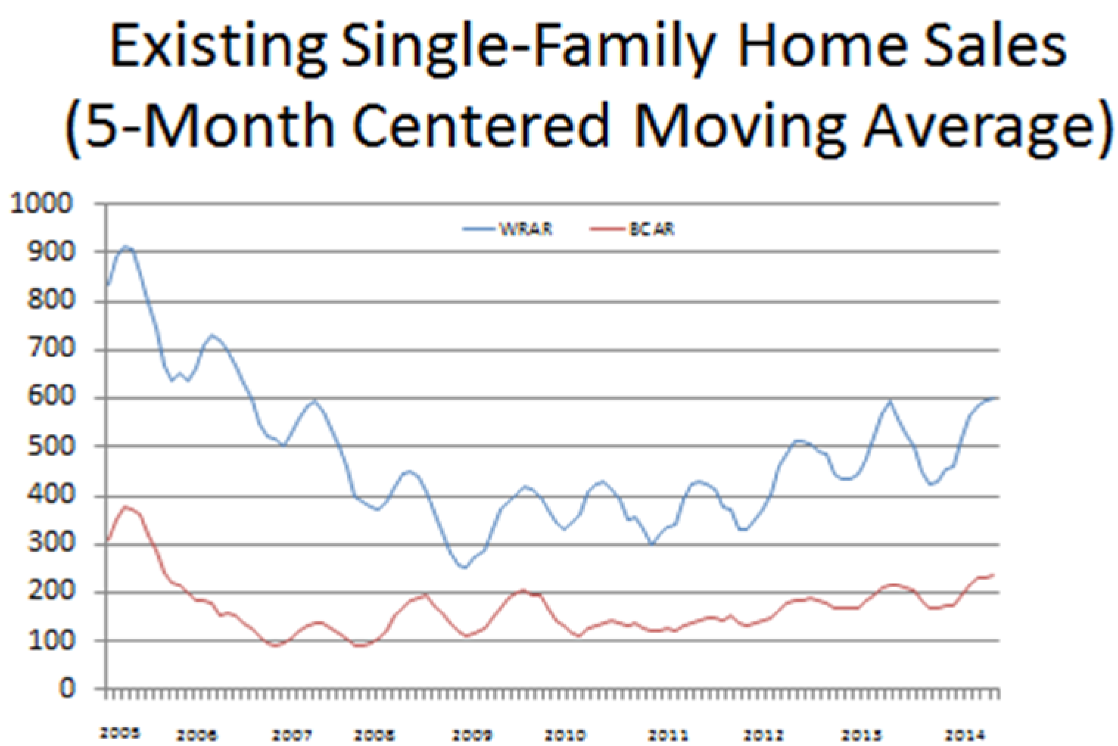
New Hanover County Room Tax Collections Growth Rates

(Not Seasonally Adjusted)



Residential Real Estate. The southeastern North Carolina residential real estate market has stabilized and resumed moderate growth. The most recent data show that sales of existing single-family homes have rebounded to their pre-recession levels. From their low reached in late 2007, sales in the area served by the Brunswick County Association of Realtors (BCAR) were up 112% as of the end of 2014. The comparable rise in the area served by the Wilmington Area Association of Realtors (WRAR) from the low reached in late 2008/early 2009 was 93%. Despite this growth, current sales in the area served by both associations are only approximately one-half of their cyclical highs which were reached in mid-2005.As of the fourth quarter of 2014, average sales prices in the BCAR and WRAR areas were up 24% and 18% from their respective lows reached in early 2012 and late 2008.

Source: NC Association of Realtors.

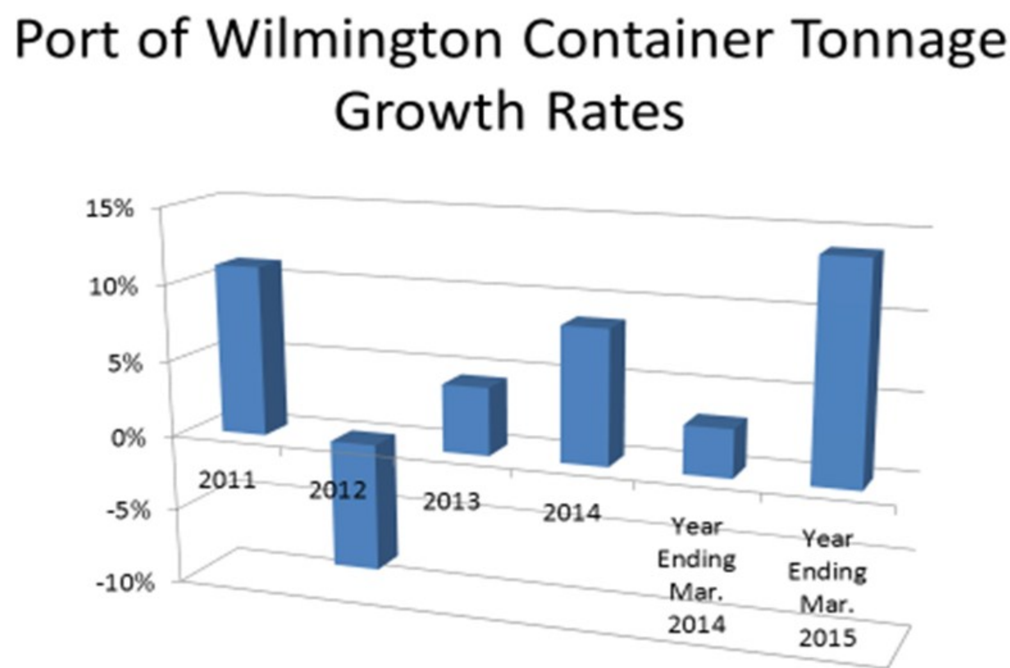


Air Passenger Traffic. Following no change in both 2012 and 2013, passenger traffic at the Wilmington International Airport fell noticeably in 2014. For the year ending March 2015 (April 2014-March 2015), passenger boardings were up 1.5%, but passenger deboardings were down 2.6%.

Source: Wilmington International Airport Manager's Office.

Port of Wilmington Container Tonnage. Following strong growth over 2011, container tonnage at the state port in Wilmington declined noticeably in 2012, only to rebound in both 2013 and 2014. For the year ending March 2015 (April 2014-March 2015), container tonnage was up 13.9%.

Source: NC State Ports Authority.



Summary. Although below the growth that occurred prior to 2008-09 recession, overall economic activity in the Wilmington, NC MSA (New Hanover and Pender Counties) is expected to grow 3.5-4% over the next two years. Area county unemployment rates are at their lowest levels in more than five years. The retail trade and tourism sectors have more than recovered from their lows reached during the most recent recession. The residential real estate market has resumed steady growth, although sales are only half of their mid-2005 levels. Two sectors which have yet to show continuing growth are container tonnage at the state port facilities at Wilmington and passenger traffic at the Wilmington International Airport.

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